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In the Supreme Court of the United States

OCTOBER TERM, 1970

No. 61

INVESTMENT COMPANY INSTITUTE, ET AL.

v.

WILLIAM B. CAMP, COMPTROLLER OF THE CURRENCY, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE COMPTROLLER OF THE CURRENCY

OPINIONS BELOW

The opinion of the district court (App. 206–247) is reported at 274 F. Supp. 624. The opinion of the court of appeals (App. 263–310) is reported at 420 F. 2d 83.

JURISDICTION

The judgment of the court of appeals was entered on June 21, 1969, and a timely petition for rehearing was denied on August 15, 1969. The petition for a writ of certiorari was filed on November 12, 1969, and was granted on March 23, 1970 (397 U.S. 986). The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether mutual funds, salesmen of mutual funds, and mutual fund investment advisers and underwriters, have standing to challenge the operation of commingled managing agency investment accounts by national banks under regulations promulgated by the Comptroller of the Currency or, assuming standing, whether these parties have a "legal interest" which entites them to protection from the statutory violations they allege.

2. Whether the operation of a commingled managing agency investment account is within the fiduciary powers granted national banks (12 U.S.C. 92a) and consistent with the prohibitions of the Glass-Steagall Act against bank involvement in the securities business (12 U.S.C. 24, 78, 377, 378).

STATUTES AND REGULATION INVOLVED

Pertinent portions of Sections 16, 20, 21 and 32 of the Glass-Steagall Act, as amended (12 U.S.C. 24, 377, 378 and 78); 12 U.S.C. 92a; and of Regulation 9 of the Comptroller of the Currency (12 C.F.R. 9), are set forth in Appendix A, *infra*, pp. 49–61.

STATEMENT

1. Petitioners, an association of mutual funds, mutual fund salesmen, and mutual fund investment advisers and underwriters, and certain members of that association, brought this action to invalidate regulations of the Comptroller of the Currency (12 C.F.R. 9.18), which permit national banks to operate commingled managing agency investment accounts on spe-

cified terms. In particular, petitioners sought to enjoin the Comptroller from permitting the respondent First National City Bank (the Bank) to operate such an account.

The complaint alleged that the operation of a commingled managing agency investment account under the Comptroller's regulations are not within the fiduciary powers granted national banks by 12 U.S.C. 92a, and is inconsistent with the prohibitions of the Glass-Steagall Act against bank involvement in the securities business (12 U.S.C. 24, 78, 377, 378). Petitioners further asserted that the "illegal activity" authorized by the Comptroller would subject mutual funds, salesmen of mutual funds, and mutual fund investment advisers and underwriters, to "illegal competition" which will "deprive them of legitimate business," cause "loss of opportunities for profit in their trade," and "dilute, divert, and withdraw a substantial portion of the potential market" for mutual fund securities and mutual fund services. Although the complaint asserted that the Glass-Steagall Act prevented mutual funds, salesmen of mutual funds, and mutual fund investment advisers and underwriters, from "expanding their operations into the commercial banking business," no claim was made that the Comptroller's regulations or action challenged here (authorizing Citibank's commingled managing agency investment account) imposed any restriction, burden, or duty upon petitioners (App. 5–17).

2. A national bank with a trust department is authorized "to act as trustee, executor, administrator,

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registrar * * *, guardian * * *, assignee, receiver, * * * or in any other fiduciary capacity in which State banks, trust companies, or other corporations which come into competition with national banks are permitted to act under the laws of the State in which the national bank is located" (12 U.S.C. 92a). The Federal Reserve Board, which regulated the fiduciary activities of national banks from 1913 until 1962, allowed national banks holding trust funds or pension, profit-sharing, or stock bonus plan funds to pool these funds together when authorized to do so by the governing instrument or by local laws.[1] Commingling allowed the pooled funds to share administration expenses, thus reducing the service and management fees charged by the bank to each individual fund, and also allowed the diversification of assets required for a sound investment program (App. 190–191).

Another longstanding fiduciary service authorized by 12 U.S.C. 92a is the "managing agency," under which the bank buys, sells and holds securities for the account of a customer as the customer's agent.[2] Before 1962, the Federal Reserve Board did not permit managing agency funds of individuals [3] to be pooled, so that it was not economically feasible for a bank to accept from individ-

[1] See 2 F.R. 2976 (1937); 20 F.R. 3305 (1955).

[2] See App. 189–190; 1934 Fed. Res. Bull. 609; 1 Scott, *Trusts* (3d ed.) § 8.1, pp. 80–81. 12 U.S.C. 24 provides in part that national banks may deal in securities and stock "upon the order, and for the account of, customers * * *."

[3] Corporate pension, profit sharing and stock bonus plan funds held by the banks in the capacity of managing agent were permitted by the Federal Reserve Board's 1955 regulation to be invested collectively. 20 F.R. 3305.

uals a managing agency account of less than $100,000, because the cost of managing a smaller account was not covered by the usual charge of approximately one-half percent annually (App. 190–191, 195–196).

In 1962 Congress transferred the supervision of the trust activities of national banks from the Federal Reserve Board to the Comptroller of the Currency. 76 Stat. 668. The Comptroller thereafter requested all affected banks to submit recommendations as to how the then existing fiduciary regulations might be improved (App. 189). The response was voluminous, and the Comptroller appointed a committee of experts to study those regulations and recommend revisions (*ibid.*; 42 Trust Bulletin No. 6, p. 10 (1963)). Based upon this committee's recommendations, new regulations were proposed covering the entire field of trust powers of national banks, and among them was a proposed authorization for the pooling and collective investment of funds held by banks in the capacity of managing agent (App. 191–192; 28 F.R. 1111 (1963)).[4] After receiving and considering com-

[4] The Federal Reserve Board had been considering a similar authorization for some time before the supervision of trust activities was transferred to the Comptroller, but the Board "had not come to the conclusion that this was a desirable thing at the time the transfer was made." Testimony of Chairman Martin, Hearings on H.R. 8499 and H.R. 9410 before the Subcommittee on Commerce and Finance of the House Committee on Interstate and Foreign Commerce, 88th Cong., 2d Sess., p. 108 (1964).

When the Board restricted the common trust fund to "bona fide fiduciary purposes" and refused to sanction commingled managing agency accounts (2 F.R. 2976(1937)), it was exercising the discretionary powers conferred upon it by 12 U.S.C. 92. The foregoing limitations were *not* based upon the Board's

ments, including those of the petitioner Investment Company Institute, the Comptroller promulgated a new set of regulations to govern all the trust activities of national banks (12 C.F.R. Part 9), and these regulations included authorization, on specified terms, for the collective investment of managing agency funds (12 C.F.R. 9.18(a)(3)).

The Securities and Exchange Commission also considered such commingled accounts from its regulatory viewpoint, and concluded that—in addition to the protections enumerated in the Comptroller's regulations and further provided by his regular bank examinations—bank customers participating in such accounts also required the protections provided by the Investment Company Act of 1940 and the Securities Act of 1933. Thus, it concluded that a commingled account should be treated as an investment company and the participants should be given certificates of interest registered with the Commission as securities (see App. 192–193).

The addition of these Commission requirements created some inconsistencies with the Comptroller's regulations. For example, the Comptroller required a bank administering such a collective investment fund

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construction of the Glass-Steagall Act. For example, in 1955 the Board permitted the commingling and common administration by banks of pension and profit sharing funds without any limitation that such funds be established for "bona fide fiduciary purposes." 20 F.R. 3305 (1955). When Congress transferred the supervision of the trust activities of national banks to the Comptroller in 1962, it vested the Comptroller with the continuing discretionary authority over trust activities that had formerly resided in the Board.

to have "the exclusive management thereof" (12 C.F.R. § 9.18(b)(12)); but the Investment Company Act contemplated governance by a board of directors, a majority of whom could not be affiliated with the managing bank (see 15 U.S.C. 80a–10(b)(3), (c)). Similarly, the Comptroller's regulations prohibited the issuance of any certificate or other document "evidencing a direct or indirect interest in such fund" (12 C.F.R. 9.18(b)(13)), while the Securities Act required certificates to be issued and registered with the Commission.

The respondent First National City Bank prepared a plan for a commingled managing agency account which the Bank believed would satisfy all of the various pertinent regulatory requirements. A customer with $10,000 or more [5] which he wished to be managed by the Bank would execute a written agreement appointing the Bank managing agent and specifically authorizing the customer's funds to be commingled with those of other customers signing similar agreements (App. 158). The customer would receive a document stating the number of "units of participation" he held as an undivided interest in the pooled fund (App. 134). The fund would be governed by a committee of five persons elected annually by the participants; the original committee would include three officers of the Bank, and it was contemplated that a

[5] This $10,000 minimum is not required by the Comptroller's regulations. The Comptroller's Office advises us that one national bank has submitted to the Comptroller and the Commission for approval a collective investment fund, similar to the one here involved, with a $5,000 minimum, and another national bank is actively considering a $2,500 minimum.

majority of the committee would continue to be Bank officers (App. 101, 153, 154–155, 202). The Bank was to be the investment adviser to the collective fund and the custodian of its assets; *for purposes of the securities laws,* the Bank would also be considered to be an underwriter of the units of participation (App. 104–108, 136–144). The units of participation would be registered with the Commission as securities (see App. 95–133) and a prospectus made available to prospective investors (see App. 146–157).

This plan was filed with and found satisfactory by the three federal agencies concerned. The Comptroller found that the Bank would be exclusively responsible for the operation of the collective investment fund and would administer it just as it would any other fiduciary service. He therefore granted to the fund a specific approval under 12 C.F.R. 9.18(c)(5), thus allowing the fund to be established with some modifications of the pattern set forth in 12 C.F.R. 9.18 (App. 194–205).[6] The Federal Reserve Board likewise viewed the fund as a part of the Bank for purposes of the banking laws, and therefore ruled that the participation of Bank officers on the committee of the fund would not be an affiliation with an issuer of or

[6] Thus Judge Bazelon's concurring opinion below noted (App. 268):

"The Bank's plan does not conform in all respects to Regulation 9 as originally issued due to the adjustments required to satisfy the requirements of the Investment Company Act. The plan, as amended, received the Comptroller's written approval under 12 C.F.R. § 9.18(c)(5), and it is expected to set the pattern for other bank-sponsored investment funds. There is accordingly no need to review the provisions of Regulation 9 as it was originally promulgated."

dealer in securities, prohibited by Section 32 of the Glass-Steagall Act, 12 U.S.C. 78 (see 12 C.F.R. 218.111).[7] The Commission concluded that certain provisions of the Investment Company Act were not intended to apply to a bank-sponsored collective investment fund, particularly in light of the additional protection provided to the fund's participants by the Comptroller's regulations. The Commission therefore granted certain exemptions from the Investment Company Act that would, *inter alia,* permit a majority of the account's governing board to be Bank officers.

In accordance with the approval granted by these three federal agencies, the Bank established a commingled managing agency account (the "Account") in 1966 and that Account is now in operation (App. 199–201). We summarize below the essential characteristics of the Account.

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[7] With respect to the question whether Section 21 of the Glass-Steagall Act applies, the Board's ruling "expressed no position," explaining that "since section 21 is a criminal statute, the Board has followed the policy of not expressing views as to its meaning." 12 C.F.R. 218.111 (k).

[8] The National Association of Securities Dealers, which had intervened before the Commission in opposition to the request for exemption, challenged the exemption in the court below. The court upheld the exemption in the same opinion in which it upheld the Comptroller's regulation. The validity of the exemption is the issue in the companion case of *National Association of Securities Dealers* v. *Securities and Exchange Commission*, No. 59, which is scheduled to be argued immediately before the present case. The Commission is not defending its order before this Court, but the Solicitor General is filing in that case a brief *amicus curiae* in behalf of the United States, in which he argues that the Commission properly granted the exemption.

3. Under the plan, a bank customer tenders his funds (between $10,000 and $500,000) to the Bank together with a broad authorization and power of attorney making the Bank the customer's managing agent. The authorization specifically provides for the Bank's investment of the customer's funds, together with the funds of other customers who have given the same authorization, through a commingled investment account. If the Bank is satisfied that the investment policy of the Account is suitable for the individual customer's needs, it accepts his money, and, as his agent, adds that money to the Account on one of the specified valuation dates.[9]

The customer's undivided interest in the Account is expressed in terms of units of participation, which are represented by a non-negotiable receipt. The customer may withdraw from the Account on any valuation date. Because of the underlying principal-agency relationship, his interest in the account terminates upon his death or incompetency, in which event his funds are withdrawn from the Account and held for his legal representatives (App. 134, 197–198, 203–204).

The custody and investment of the customer's funds are handled by the Bank pursuant to a management agreement between the Bank and the Account. The funds are invested, within certain guidelines, in accordance with the broad discretionary directions of the trust department officer or officers assigned to the Ac-

[9] The market value of the assets of the fund is computed regularly, so that the net value of each unit of participation can be established. Each such computation is made on a valuation date (App. 204).

count. The Comptroller's regulations limit the total compensation of the Bank to the sum of the fees it would normally charge its customers for separate management of their accounts. The Bank's compensation is limited to a sum equal, on an annual basis, to one-half percent of the average net asset value of the Account.[10] Unlike the situation of most mutual funds—where the investor pays a sales charge and underwriters, brokers, and securities dealers make profits from the distribution of mutual fund shares—the customer-investor under the instant plan pays no charge for participating in the Account, nor does the Bank or anyone else receive any commission or other profit for arranging the participation (App. 136–142, 198–199, 202–205).

Moreover, unlike most mutual funds—which are aggressively marketed through all channels of public distribution by investment companies, their principal underwriters, brokers, and securities dealers[11]—partici-

[10] Most mutual fund investment advisers make a similar charge. Unlike the bank's fund, however, mutual fund advisory fees usually do not include costs of charges for "stock transfers, dividend disbursing, and custodial services, the most substantial nonadvisory services required by mutual funds * * *." Report of the Securities and Exchange Commission on Public Policy Implications of Investment Company Growth, H. Rep. No. 2337, 89th Cong., 2d Sess. 10 (1966). In addition, most mutual funds also charge a sales fee or "load" constituting a percentage of the amount invested (*id.* at 19).

[11] "Principal underwriters [of mutual funds] use two different distribution techniques. Some confine themselves to wholesaling and leave the actual selling to independent retail dealers. Others have their own retail sales organization called "captive sales forces." In either case, the growth of the funds through the sale of new shares increases the advisory, the underwriting and, in an appreciable number of instances, the brokerage income of those who control them." H. Rep. No. 2337, *supra*, p. 11, fn. 10, at 9.

pation in the Account is offered only by the Bank itself as a part of its fiduciary services. There is no public distribution of participations in the Account through underwriters, brokers, dealers or any other marketing agency. The Account merely agrees to make units of participation available to customers of the Bank upon request of the appropriate officer. The Comptroller's Regulation prohibits advertising a collective investment account, except in connection with the Bank's general fiduciary services. The Regulation also limits the Bank's publicizing of its investment record.

The Account, like other banking functions, is subject to the constant examination and supervision of the Comptroller, including scrutiny of the Account's investments. The Comptroller's Regulation preserves the fiduciary character of the Bank's relationship to its customers by requiring the separation of the Account's funds from other assets, by barring the Bank from possessing any interest in the Account, and by enforcing other normal fiduciary obligations such as avoidance of self-dealing and conflicts of interest (App. 141, 198–200, 202, 204–205, 269–270; 12 C.F.R. 9.11(d), 9.18; 12 U.S.C 481).[12]

[12] Petitioners state (Br. 45, fn. 51) that the restrictions of Section 9.18(b) of the Comptroller's Regulation "appear to be inapplicable to funds like those of Citibank." While the Comptroller allowed the Bank's fund to be established with some modifications of the pattern set forth in Section 9.18, he specifically stated that "all of the protections deemed necessary by this Office," provided by Section 9.18(b), must be

The Comptroller and the Federal Reserve Board concluded that the essential nature of the commingled account is not altered by the additional safeguards

complied with (App. 205). The specific changes in operation allowed by the Comptroller are listed below.

1. Section 18(a)(3) of Regulation 9, 12 C.F.R. 9.18(a)(3), provides for the operation of a commingled account as a common trust fund for funds received by the bank as managing agent under an express trust agreement. The Account as established does not provide for an express trust agreement; rather, each customer deposits his funds with the bank together with a broad power of agency specifically authorizing the bank to deposit those funds in the Account and to invest and reinvest them at its discretion (App. 159). See Pet. Br. pp. 53–55.

2. Section 18(b)(12), 12 C.F.R. 9.18(b)(2), provides that the bank administering a commingled account shall have the exclusive management thereof. The Account as established is supervised by a committee, elected annually by the participants, which enters into an agreement with the bank for the management of the Account (see *infra*, p. 14). In the four years of operation of the Account, this committee has always contained a majority who were officers of the Bank's Trust and Investment Department (see App. 198).

3. Section 18(b)(5), 12 C.F.R. 9.18(b)(5), provides for audit by auditors responsible only to the board of directors of the bank. In accordance with the provisions of the Investment Company Act, the Account as established provides for the annual approval of the auditors by vote of the participants. 15 U.S.C. 80a–31.

4. Section 18(b)(13), 12 C.F.R. 9.18(b)(13), forbids the issuance of any certificate or other document evidencing a direct or indirect interest in a common trust fund. The Account as established requires the issuance of a receipt showing the units of participation credited to a customer's account. These receipts are not negotiable.

Although the Comptroller allowed changes in the operation of the Account in order to satisfy the requirements of the Investment Company Act, the Account still retained the essential characteristic envisaged by the Comptroller's regulations and

which were established to satisfy the Securities and Exchange Commission and the requirements of the Investment Company Act (App. 192–193; 205; 12 C.F.R. 218.111; App. 278, 309–310). These additional safeguards are: (a) The Account is supervised by a five-member committee originally appointed by the Bank and elected annually by the participants in the Account. (b) The Investment Company Act required two of the five members of the committee to be unaffiliated with the Bank (App. 269), although the majority of the committee has been, and is expected to be, controlled by the the Bank. (c) The committee enters into an agreement with the Bank for the Bank's management of the Account, which agreement may be cancelled by a majority of the committee at any time (App. 141). (d) The management agreement, whose terms are detailed above, *supra,* expires annually unless renewed upon majority vote of the participants or of the committee (including a majority of the non-Bank affiliated members), and is otherwise subject to conditions imposed by the Investment Company Act of 1940 (App. 141; 15 U.S.C. 80a–15). (e) The investment policy of the Account may be changed only by a majority vote of the participants (15 U.S.C. 80a–13).

Within the broad outlines of the Account's fundamental investment policy, however, the Bank, until

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was, of course, approved by the Comptroller. The protections extended to a customer whose money is accepted by the Account are, by virtue of the subjection of the Account to the Investment Company Act requirements, even greater than they would be if the Account were under the exclusive direction of the Comptroller. See *supra*, p. 14.

such time as its management agreement is cancelled or expires without renewal, retains exclusive control of the Account.

4. After the Account was established, petitioners brought this action in the district court for declaratory and injunctive relief, seeking to have the Comptroller's regulations declared unlawful and the operation of the Account prohibited. The district court granted petitioners' motion for summary judgment, holding that "the provisions of Regulation 9 which allow commingling of managing agency accounts do not comply with the statutory provision [*sic*] of the Glass-Steagall Act and are, therefore, illegal" (App. 247).

The court of appeals unanimously reversed (Pet. App. 2a–3a). In a brief *per curiam* opinion, the court stated that, "[o]n the merits, we are agreed that the actions taken by the Securities and Exchange Commission and the Comptroller are fully consonant with the statutes committed to their regulatory jurisdictions" (App. 266). The members of the panel went on to elaborate their views in separate concurring opinions, one by Chief Justice (then Judge) Burger, with whom Judge Miller joined, and another by Chief Judge Bazelon.

Judge Burger's opinion stated (App. 309–310):

> Our review function is narrow and limited; it does not include the power to decide whether the public will be better served by one or the other modes of investing funds so as to achieve diversifications, yield, safety or low cost. All

> that is the primary responsibility of the special regulatory bodies established by Congress for that purpose. * * *
>
> Here, the Comptroller of the Currency, after study, has decided that the commingled managing agency account is a function which is authorized by law for banks and is in the public interest; the Securities and Exchange Commission and the Federal Reserve Board have approved. Other state and federal regulatory bodies are in accord. The regulatory bodies charged by Congress with these large responsibilities have construed the grant of power and with their accumulated expert experience have decided these issues. Their decisions are entitled to substantial deference and on this record I see no basis for disturbing their conclusions.

Judge Bazelon's opinion discussed in detail each of the aspects of the case (App. 266–286), and concluded that "the [commingled managing agency] Account, subject to the mutually reinforcing regulations imposed by the Comptroller and the Commission, was established in accordance with law" (App. 267).[13]

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[13] While Judge Burger and Judge Miller expressed their "grave doubts" as to petitioners' standing to maintain the action, they nevertheless resolved those doubts in petitioners' favor (App. 309). Judge Bazelon was of the view that petitioners have standing (App. 286–296). The decision in this case was rendered prior to this Court's elaboration of the standing and "legal interest" requirements in *Association of Data Processing Service Organizations* v. *Camp*, 397 U.S. 150 ("ADAPSO"). In Point I of the Argument, we urge that petitioners cannot meet the standing and "legal interest" requirements set forth in *ADAPSO*.

SUMMARY OF ARGUMENT

Petitioners—mutual funds, salesmen of mutual funds, and mutual fund investment advisers and underwriters—brought this action to challenge the right of national banks to operate commingled managing agency investment accounts pursuant to a regulation promulgated by the Comptroller of the Currency. They contend that the performance of such service is not within the fiduciary powers granted national banks (12 U.S.C. 92a) and is inconsistent with the prohibitions of the Glass-Steagall Act against bank involvement in the securities business (12 U.S.C. 24, 78, 377, 378).

I. Petitioners have no standing to maintain this suit. They complain that the effect of national bank activity in this area will be to provide competition to mutual funds. They do not contend that the Comptroller is attempting to regulate their own activities in any fashion or that they are threatened with any injury other than competitive.

The sole purpose of the Glass-Steagall Banking Act of 1933, upon which petitioners rely, was to protect the banking public through the maintenance of a sound national banking system. Congress did not intend to confer any benefits upon, or to afford any protection to, mutual funds or any others in the securities field. In such circumstances, petitioners lack standing to challenge the operation of a commingled managing agency investment account, for the interest sought to be protected by petitioners is not "arguably within the zone of interests to be protected or

regulated" by the Glass-Steagall Act or any other relevant statute. *ADAPSO, supra,* 397 U.S. 150, 153. In any event, under this Court's decision in *ADAPSO,* 397 U.S. at 153, the judgment below must be affirmed on the ground that petitioners have no legal interest which protects them from the statutory violations which they allege, and therefore are not entitled to obtain judicial relief on the basis of those statutory claims.

II. Operation of a commingled managing agency investment account is consistent with the prohibitions of the Glass-Steagall Act against bank involvement in the securities business, because participating interests in the Account are not "securities" within the meaning of that Act. The definition of "securities" in the securities laws is inapplicable to the banking laws. As Judge Bazelon noted in the court below (App. 274), the term "security" in the Securities Act of 1933 is a "term of art with a high gloss", whose "expansive definition under the Securities Act cannot be imported wholesale into the Glass-Steagall Act when the two statutes serve different purposes * * *."

The proper line of inquiry in this case is not whether the certificates issued to participants in the Account are securities under the securities laws, but instead whether operation of the Account is consistent with the purposes of the Glass-Steagall Act. The legislative history of the Glass-Steagall Act demonstrates that Congress attempted in that Act to separate commercial and investment banking, and to safeguard

commercial banks from making excessively speculative financial commitments, which were fraught with potential conflict of interest problems, by prohibiting banks from purchasing, issuing and underwriting securities. The Act was not intended to limit the traditional function of banks to manage the investments of their customers in a fiduciary capacity, whether through individual or commingled accounts. The Account here, which simply makes available to the smaller investor the benefit of investment management by a bank trust department which was formerly available only to large investors, presents, as Judge Bazelon noted, no potential problems which are not present "in all bank investments in securities for the account of customers" (App. 275). Since these problems were not those that Congress had in mind when it enacted the Glass-Steagall Act, operation of the Account does not violate the purposes of that Act.

III. Once it has been determined that operation of the Account is not inconsistent with the purposes of the applicable banking statutes, the complex questions about the appropriateness of such accounts in general and the details of their operation are questions for the regulatory agencies charged with administration of the banking laws. As Judge Burger noted in his concurring opinion below, the Comptroller and the other regulatory bodies have considered the issues presented here with "their accumulated expertise", and in view of the fact that they have not exceeded their statutory discretion, there is "no basis for disturbing their conclusions" (App. 310).

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ARGUMENT

I

PETITIONERS—MUTUAL FUNDS, SALESMEN OF MUTUAL FUNDS, AND MUTUAL FUND INVESTMENT ADVISERS AND UNDERWRITERS—HAVE NO STANDING TO CHALLENGE THE OPERATION OF COMMINGLED MANAGING AGENCY INVESTMENT ACCOUNTS BY NATIONAL BANKS UNDER REGULATIONS PROMULGATED BY THE COMPTROLLER. IN ANY EVENT, PETITIONERS HAVE NO LEGAL INTEREST WHICH PROTECTS THEM AGAINST THE STATUTORY VIOLATIONS WHICH THEY ALLEGE.

Even though these issues were extensively considered below, petitioners make no attempt in their brief in this Court to demonstrate either that they have standing to maintain this action or that, assuming standing, they have a "legal interest" which entitles them to relief from the statutory violations they allege. But this Court's recent decision in *Association of Data Processing Service Organizations* v. *Camp*, 397 U.S. 150 (hereafter "*ADAPSO*") plainly requires consideration of these issues.[14]

ADAPSO held that the standing of a plaintiff to attack governmental action assisting a competitor depends upon (1) the existence of a case or controversy (for which "injury in fact" is sufficient); and (2) "whether the interest sought to be protected by the

[14] The Court noted in *ADAPSO* (397 U.S. at 157, fn. 2): "We intimate no view, under the decisions rendered today here and in Barlow v. Collins * * * [397 U.S. 159] on the issue of standing involved in No. 835, National Association of Securities Dealers v. SEC, and No. 843, Investment Company Institute v. Camp, now pending on petitions for writs of certiorari."

complainant is arguably within the zone of interests to be protected or regulated by the statute or constitutional guarantee in question" (397 U.S. at 153). In other words, this Court in *ADAPSO* concluded that the ultimate test of standing was neither "aggrievement in fact" (as contended by *ADAPSO, id.* at 152) or "legal interest" (as contended by the government) but, rather, was something in between the two: "arguably within the zone of interests."

However, while rejecting "legal interest" as a test of *standing,* the Court ruled that, in order *to obtain relief* on the basis of an alleged violation of a statute, the plaintiff must establish that it has a "legal interest" which merits protection from such a violation (397 U.S. at 153, 158). The Court also indicated that the question of the existence of such a "legal interest" was independent of the question whether a statutory violation had in fact occurred. *Ibid.* In short, far from rendering irrelevant the issue of the plaintiff's legal interest in the enforcement of the statute involved, the Court simply determined that legal interest is an inquiry addressed "to the merits" rather than to standing. *Ibid.*[13]

In the instant case, which was decided by the court of appeals before this Court's opinion in *ADAPSO,* Judge Burger's majority concurring opinion stated

[13] Specifically, the Court stated that the merits involve two questions: (1) "[w]hether anything in the [relevant statutes] gives petitioners a 'legal interest' that protects them against violations of those [statutes]" and (2) "whether the actions of [the Government officials] did in fact violate [those statutes]." 397 U.S. at 158.

that he was unable to set aside his "grave doubts" as to petitioners' "standing to institute and maintain these suits" (App. 309). He discussed petitioners' standing in terms of the "legal interest" test, and concluded (App. 307–308):

> [Petitioners] here pursue their associational livelihood in a securities marketing industry which thrives on competition in the quest for the investment dollar. The entry of the national bank commingled investment accounts into this competition admittedly adds a whole new category of competitors but it is fundamentally not different from the situation which arises, for example, when "gas stations" sell candy bars, soft drinks and other staples for which travellers have need. Nevertheless, before [petitioners] may sue to prevent bank competition which affects their private financial interest, they must establish that the Glass-Steagall Act contemplated that they were to be protected from this competition in their pursuits. Even assuming that the competing activity of the Appellant Bank may be otherwise violative of a provision of the Act. *I can find no indication that the Act intended to afford protection to securities dealers generally.* My position therefore is one of reservation amounting to virtual disbelief in any standing in [petitioners]. [Emphasis added.]

The same opinion also concluded (App. 305; emphasis added):

> * * * the Glass-Steagall Act does not contain the familiar provisions which constitute an aid to standing in terms of allowing a "person ag-

> grieved" to challenge administrative decisions or promulgations made pursuant to the Act. Nor can [petitioners] validly assert any "license, grant, or recognized property interest" entitling them to standing. *It is equally clear that giving even the broadest reading of the legislative history embellishing the Act will not support the conclusion that Congress meant to bestow upon [petitioners] any protection from competitive injury.* * * *

Judge Bazelon's separate opinion agreed that "the Glass-Steagall Act was not intended by Congress to protect mutual funds from competition from banks, so they do not have standing as intended beneficiaries; and the Act contains no aggrieved party provision." (App. 287).[16]

We submit that the foregoing conclusions as to the interests protected or regulated by the Glass-Steagall Act were sound. Thus, petitioners lack standing to challenge the managing agency investment accounts by national banks, for the interest petitioners assert is not even "arguably within the zone of interest to be protected or regulated" by the Glass-Steagall Act or any other relevant statute. *ADAPSO,* 397 U.S. at 153. In any event, we submit that, as the majority concurring opinion below concluded, petitioners have no "legal interest" which protects them from the statu-

[16] Both Judge Burger's and Judge Bazelon's opinions concluded, for different reasons, that petitioners had standing. (App. 287, 294, 309). However, we show below (pp. 24, *ff.*), this Court's subsequent decision in ADAPSO precludes the grant of standing or of substantive relief on the basis of those reasons.

tory violations which they allege.[17] Consequently, under this Court's decision in *ADAPSO,* petitioners are not entitled to obtain relief on the basis of those statutory violations.

1. Petitioners seek to invalidate a regulation of the Comptroller and action by him which imposes no restriction, burden or duty upon them. Petitioners' sole basis for seeking judicial relief is their fear that, if the Comptroller's action [18] is allowed to stand, prospective customers of mutual funds (who cannot afford the same financial services from banks now enjoyed by large individual managing agency accounts) may instead invest in the bank's fund. But petitioners' wish to be free from this new competition, while understandable, is not a sufficient basis for obtaining judicial relief. As the majority concurring opinion

[17] In our brief in opposition (p. 2, fn. 1), we reserved the right to urge, as an alternative basis for affirmance, that petitioners lack standing to sue. Since our standing argument encompassed the "legal interest" test, which *ADAPSO* removed to the merits, our brief in opposition necessarily preserved the legal interest issue as well.

[18] Although petitioners purport to challenge portions of the Comptroller's regulation (12 C.F.R. 9.18) relating to commingled funds (App. 9), the commingled managing agency account of First National City Bank attacked by the complaint does not comply in full with that regulation and was granted a specific exemption by the Comptroller (App. 201–205). As already noted (*supra*, pp. 6–8, 13–14), this exemption permitted compliance with the securities laws. Without such compliance there could be no issuance of securities and thus no questions arising under the Glass-Steagall Act—the statute petitioners allege to be violated. Indeed, Judge Bazelon suggested that since the alleged illegality arises from an express exemption from the regulation, there is "* * * no need to review the provisions of Regulation 9 as it was originally promulgated." (App. 268).

and Judge Bazelon's opinion both noted (App. 287, 305), there is no "person aggrieved" provision in the governing statutes. Moreover, as the majority concurring opinion also recognized, petitioners cannot validly assert any "license, grant, or recognized property interest" (App. 305).

Thus, in order to establish a protected zone of interest, petitioners must show that Congress, in the Glass-Steagall Act or other relevant statutes, intended directly or indirectly to protect mutual funds from competition by national banks. See *ADAPSO,* 397 U.S. at 153-155, 158. See also *Hardin* v. *Kentucky Utilities Co.,* 390 U.S. 1, 5–7. Similarly, petitioners must show, in the statutory scheme, a legal interest which protects them against the statutory violations which they allege.[19] Petitioners can make no such showing.

2. The substantial increase in bank insolvencies after 1924 and other unsound banking conditions contributed substantially to the economic breakdown of 1929. Beginning with Senate Resolution 71, 71st Cong., 2d Sess. (1929), Congress sought to find means of providing "for a more effective operation of the national and Federal reserve banking systems of the country * * *." The Glass-Steagall Act of 1933, 48 Stat. 162, was enacted to correct the banking "evils which reached a peak of danger in 1929 and abuses

[19] This Court in *ADAPSO* defined "legal interest" by quoting its statement in *Tennessee Power Co.* v. *TVA*, 306 U.S. 118,-137–138, that a legal right was "one of property, one arising out of contract, * * * or one founded upon a statute which confers a privilege." 397 U.S. at 153.

which have gradually grown up within the banking system itself"; it was designed to "correct manifest immediate abuses, and to bring our banking system back into a stronger condition." Sen. Rep. No. 77, 73d Cong., 1st Sess., p. 2 (1933).

Generally speaking, the Glass-Steagall Act erected safeguards against a number of banking abuses, strengthened the hands of the bank supervisory agencies, increased the controls over the volume and use of bank credit, and provided for the insurance of bank deposits throughout the country. As particularly relevant here, several sections of the Act dealt with abuses resulting from the intermingling of the commercial and savings bank business with the underwriting and flotation of security issues and from the use of "securities affiliates"—organizations either owned by or under common control with banks, and engaged in the investment and underwriting business (Section 20).[20]

[20] These securities affiliates were organized because of the common law prohibition against the investment by a bank of its own funds in common stocks, and were designed to be controlled by the bank with which they were affiliated. Through the medium of bank loans to the affiliate secured by the securities held by the affiliate, or by bank credit to the affiliate, these organizations utilized the money held by the bank to "devote themselves in many cases to perilous underwriting operations, stock speculation, and maintaining a market for the banks' own stock * * *." Sen. Rep. No. 77, 73rd Cong., 1st Sess., p. 10 (1933). The underwriting in which the affiliates engaged was the so-called "firm-commitment" or wholesale underwriting, see 1 Loss, *Securities Regulation*, pp. 159–171 (2d ed.), in which the risk of loss rested on the affiliate. The affiliates undertook, for their own account as principals, operations in the securities market which were highly speculative—by engag-

Specifically, section 20 was designed to require the break-up of the securities affiliates, Section 21 to force the private banks out of either the banking or investment banking fields, and Section 32 to ensure that no person with a financial interest in selling securities could serve in a position where he might influence a bank's purchase of securities for itself or for its customers. See *Board of Governors* v. *Agnew,* 329 U.S. 441, 449. Section 16 was intended to confine the securities dealings of the banks within traditional bounds of agency. See S. Rep. 77, 73d Cong., 1st Sess., pp. 16–18; H. Rep. No. 150, 73d Cong., 1st Sess., p. 204.

As the majority concurring opinion below noted (App. 305), "The thrust of the legislation, and the concern of the drafters, was to protect the banking

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ing in high leverage short-term transactions, by utilizing the bank's money to engage in "market support" operations for dubious stocks and other securities held by them, or simply by making high risk investments. See 1920 Report of the Comptroller of the Currency quoted in Hearings Pursuant to S. Res. 71 before a Subcommittee of the Senate Committee on Banking and Currency, 71st Cong., 3d Sess., pp. 1067–1068.

Congress was also concerned about the existence of the "private bankers," which operated as partnerships and were, in many instances, unregulated by the States or by the Federal government. These houses were not restricted as to the investment of their own funds, and consequently could deal in stocks as well as debt securities. Further, they could operate in competition with commercial banks, accepting deposits and other accounts. Stated otherwise, these private bankers could engage, as partnerships, in all the activities for which commercial bankers were required to utilize investment affiliates, and thus were equally dangerous to the banking system. Indeed, the possibility of conflict of interest was even more direct, since both the banking and sale functions were combined in one organization. See 75 Cong. Rec. 9910–9911 (remarks of Senator Bulkley, May 10, 1932); S. Rep. No. 1455, 73d Cong., 2d Sess., pp. 221–229.

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public through the maintenance of a sound national banking system"; it was "not focused on protecting the investing public, much less the securities industry." Judge Bazelon's opinion likewise noted that: "The intended benficiaries of the banking laws, if that class is narrower than the public, are bank customers * * *" (App. 294). Senator Bulkley, one of the managers of the bill, stated this explicitly during the debates:

> [T]he purpose of this bill does not extend to safeguarding purchasers of securities as such. The purpose of this bill is to improve the operation of the Federal Reserve system and the banks which are members of it. The object of the inhibitions which I am discussing here is not primarily to protect the investing public, although that is a worthy purpose, but our field is to protect the operations of the banking system itself, and to protect the depositors and customers of the banks so that they shall have the service from national and State member banks which they are entitled to expect.

75 Cong. Rec. 9913–9914 (1932).[21]

In particular, Congress discerned that the intermingling of commercial and investment banking, and

[21] See also 75 Cong. Rec. 9914 (May 10, 1932) (remarks of Senator Bulkley) ("* * * the measure as a whole is in all of its fiber intended as a protection for depositors"); 75 Cong. Rec. 9915 (May 10, 1932) (remarks of Senator Glass) ("* * * it is not a safe business for a commercial bank to be engaged in investment banking. They ought to be entirely separate").

the practice of "security affiliates," threatened the maintenance of a sound national banking system by: (a) contributing to bank failures; (b) endangering the safety of bank deposits; (c) leading to conflicts of interests by bankers; (d) inducing the making of unsound bank loans; (e) impairing public confidence in the banking system; and (f) diverting the resources of the commercial banking system to speculative purposes never contemplated by Congress. A detailed account of the problems which led to the enactment of the Act is set forth in Appendix B to this brief.

There was no Congressional objective to protect mutual funds or their investment advisers or underwriters. Indeed, one of the arguments *against* the bill was that it would "throw the issue of securities back into the hands of private bankers little subject to public authority," and give the investment bankers a "monopoly." See 75 Cong. Rec. 10002 (May 11, 1932); 77 Cong. Rec. 3958 (May 22, 1933). Congress was concerned that, when the commercial banks were withdrawn from the investment business, there should remain adequate facilities to serve the needs of that industry. 75 Cong. Rec. 9913 (May 10, 1932) (colloquy between Senator Vandenberg and Senator Bulkley); 77 Cong. Rec. 3955, 3957 (May 22, 1933) (remarks of Rep. Bacon). But nowhere in the extensive legislative history of the Glass-Steagall Act can there be found even a suggestion that one of the Congressional purposes was the protection of those in the securities or invest-

ment field, or the conferring upon them of any legal right to be free from competition."[23]

3. The foregoing review of the legislative purpose of the Glass-Steagall Act shows that petitioners lack standing to challenge the operation of commingled managing agency investment accounts by national banks. The interest sought to be protected by petitioners is not even "arguably within the zone of interests to be protected or regulated" by the Glass-Steagall Act or any other relevant statute, *ADAPSO*, 397 U.S. at 153. If, as Senator Bulkley stated (*supra*, p. 28), the purpose of the legislation was "not primarily to protect the investing public," *a fortiori* it was not to protect members of the securities industry engaged in selling to the public.

In any event, petitioners certainly cannot demonstrate a legal right or interest "* * * founded on a statute which confers a privilege." *ADAPSO, supra*, 397 U.S. at 153, quoting from *Tennessee Power Co.* v. *TVA*, 306 U.S. at 137. Neither the Glass-Steagall Act nor any other relevant statute confers upon mutual funds or the investment business any right to protection against the competition of national banks. Since petitioners have no other basis for claiming a "legal interest" which protects them from the statutory violations which they allege, they are not entitled to obtain judicial relief here.

[23] Indeed, the Congressional attitude toward the investment bankers can only be characterized as one of distaste. For example, in discussing the private investment bankers, Senator Glass pointed out that many of them had "unloaded millions of dollars of worthless investment securities upon the banks of this country * * *." 77 Cong. Rec. 4179 (May 25, 1933).

The court below agreed with our analysis of the legislative purpose of the Glass-Steagall Act. The majority concurring opinion, however, resolved its doubts against standing in favor of petitioners because of "the need for judicial examination of the important questions raised" (App. 309).[23] This Court's decision in *ADAPSO,* however, makes it clear that the importance of the questions raised cannot confer standing upon a plaintiff, or permit a plaintiff to

[23] As a practical matter, Congressional examination of the questions presented would seem to diminish the need for judicial examination. Congress has previously considered, and currently has under review, the question of national bank operations of commingled managing agency investment accounts. See S. 2224, 91st Cong., 1st Sess.; 115 Cong. Rec. 13700 (May 26, 1969); H.R. 17333, 91st Cong., 2d Sess.; H.R. 6778, 91st Cong., 1st Sess.; 115 Cong. Rec. H10554, H10559 (Daily ed. Nov. 5, 1969). See also Hearings on Bank and Insurance Company Collective Investment Funds and Accounts, Investment Company Act Amendment of 1967, H.R. 14742 before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce, 90th Cong., 2d Sess. (1968); Hearings on Amendment No. 438 to S. 1659 before the Senate Comm. on Banking and Currency, 90th Cong., 1st Sess. (1967); Hearings on S. 2704 before a Subcomm. of the Senate Comm. on Banking and Currency, 89th Cong., 2d Sess. 582 (1966); Hearings on H.R. 8499 and H.R. 9410 before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce, 88th Cong., 2d Sess. 49 (1964). See *Arnold Tours, Inc.* v. *Camp*, C.A. 1, No. 7192, decided June 1, 1970, on remand Slip Opin., p. 4, fn. 4 (Aldrich, Ch. J.): "* * * the fact that Congress is considering the question * * * might suggest an additional reason for our ruling against the plaintiffs. Then, if we have misunderstood the intent of Congress, it may correct us."

obtain relief on the basis of an alleged statutory violation if plaintiff cannot establish that it has a "legal interest" in protecting him from such a violation.[24]

II

THE OPERATION OF A COMMINGLED MANAGING AGENCY INVESTMENT ACCOUNT IS CONSISTENT WITH THE PROHIBITIONS OF THE GLASS-STEAGALL ACT AGAINST BANK INVOLVEMENT IN THE SECURITIES BUSINESS, BECAUSE PARTICIPATING INTERESTS IN THE ACCOUNT ARE NOT "SECURITIES" WITHIN THE MEANING OF THAT ACT.

Petitioners contend that operation of the Account violates Sections 16, 20, 21 and 32 of the Glass-Steagall Act, 12 U.S.C. 24, 377, 378 and 78, which limit banks to purchasing and selling "securities" only for the account of customers, and which prohibit direct or indirect affiliations between banks and issuers, underwriters, sellers or distributors of "securities". Petitioners' case is premised almost entirely on the argument that the "units of participation," represented by the certificates which the Bank gives to participants, are "securities" under the Glass-Steagall Act.[25] For the reasons set forth below, we believe that

[24] Judge Bazelon's opinion concluded that it "is fortuitous that there is no aid to standing for these plaintiffs," and that the "absence of a statutory aid to standing in this case is adventitious and I would grant appellants standing to assert the public interest without it" (App. 287, 294). Since, however—as Judge Bazelon himself recognized—Congress indicated the interests it intended to protect by the passage of the Glass-Steagall Act, the absence of a congressionally established zone of interest or "legal interest" may not—consistent with this Court's decision in *ADAPSO*—be ignored as "adventitious" or "fortuitous."

[25] Petitioners devote relatively little space in their brief, and seem almost to have abandoned, their contention below that the

petitioner has attempted here to impose on the Glass-Steagall Act a definition which belongs peculiarly to the securities regulation statutes, and that the issuance of interests in the Account does not constitute dealing

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commingled managing agency account is not authorized by 12 U.S.C. 92a, which permits national banks to engage in fiduciary activities, on the ground that operation of the Account is not a fiduciary activity (Pet. Br.). In any event, the contention is not persuasive. The Comptroller's regulations require that a bank operating a collective investment fund maintain a written plan stating " * * * the manner in which the fund is to be operated, including provisions relating to the investment powers of the bank with respect to the fund * * *" 12 C.F.R. 9.18(b)(1). The Comptroller examines all banks operating collective investment funds to assure " * * * the protection of the interests of the beneficiaries and other parties at interest * * *", and, for a breach of its fiduciary duty to follow its plan, all the resources of the bank can be reached in a proper case. Hearings on Collective Investment Funds before the Subcommittee on Finance of the House Interstate and Foreign Commerce Committe, 88th Cong., 2d Sess., p. 78 (1964). All partici- that fidciary safegards have not "* * * been supplanted, insofar as funds registered under the Investment Com- ~~planted, insofar as funds registered under the Investment Com-~~ pany Act are concerned, by the obligation to adhere to the terms of the fund's prospectus." Pet. Br. p. 44. Thus the Bank is acting in a "fiduciary capacity" within the meaning of 12 U.S.C. 92a. See *Brown* v. *Christman*, 126 F.2d 625(C.A.D.C.); Restatement of Agency (Second), §§ 13, 14B and comment a; 1 Scott, *Trusts* (3d ed.) § 8.

This conclusion is not undermined, as petitioners contend (Br. 53–55), because the bank lacks in practice discretion to invest the customer's funds in any investment other than the Account. Such lack of discretion may also be true of a bank's individual managing agency account, depending upon the instructions given by the principal, but that does not alter the fiduciary nature of such an account. Moreover, since 12 U.S.C. 92a provides that national banks may act as trustee, executor, administrator, registrar, assignee, receiver "or in any other fiduciary capacity" in which competitive corporations are permitted to act, there is no merit

parts in the account continue to receive these protections, to

in securities within the meaning of the Glass-Steagall Act.[26]

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in petitioners' contention (Br. pp. 53–55) that the bank's commingled investment account is not a fiduciary activity because it lacks "personal trust concepts." The Comptroller has not, as petitioners assert, equated the terms "fiduciary" and "trustee" but instead has by regulation defined "fiduciary" as meaning "* * * a bank undertaking to act alone or jointly with others primarily for the benefit of another in all matters connected with its undertaking and includes trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, committee of estates of lunatics, managing agent and any other similar capacity." 12 C.F.R. 9.1(b). The testimony of Comptroller Saxon and Mr. Reese Harris of Manufacturers Hanover Trust Company, relied upon by petitioners (Br. 53–54), did not concern what was or was not a fiduciary relationship, but rather was directed to the characteristics which made a commingled trust account established in accordance with 12 C.F.R. 9.18(a)(1) of the Comptroller's regulation (as promulgated in 1963, 28 F.R. 3311) exempt from registration as an investment company under the Investment Company Act of 1940. Moreover, there is no question but that the activity under consideration here is open to competing state banks under New York law, as required by 12 U.S.C. 92a. New York Banking Law, § 100–c; *Brooklyn Trust Co.* v. *Corwin*, 5 F.Supp. 287, 289 (E.D. N.Y.). Indeed, subsequent to the decision below in this case, the New York State Banking Department formally approved the commingling of managing agency accounts in New York (App. 271). Therefore, we believe that no serious question can be raised concerning a violation of 12 U.S.C. 92a.

[26] Since, as will be shown below, the units of participation are not "securities" within the meaning of the Glass-Steagall Act, the merits of this case can be resolved without considering the meaning of such terms as "issue" or "underwrite" as used in that Act.

A. THE DEFINITION OF "SECURITIES" IN THE SECURITIES STATUTES IS INAPPLICABLE TO THE BANKING LAWS

The issuance of the certificates that petitioners now call "securities" is not an inherent aspect of a bank's operation of a collective managing agency account. Indeed, the Comptroller's regulations prohibit the issuance of such certificates, 12 C.F.R. 9.18(b)(13), and the only reason for their existence—and the Comptroller's special permission therefore—is the Commission's determination that the Account is subject to the Investment Company Act of 1940 and the Securities Act of 1933. The certificates (which are not transferable) merely indicate the amount of undivided interest each participant has in the commingled account (App. 134). The fact that the Commission requires, for its own regulatory purposes, the issuance and registration of these certificates is irrelevant to the question whether the operation of the Account is equivalent to doing a prohibited "securities" business within the meaning of the Glass-Steagall Act.[27]

Indeed, petitioners argument is fundamentally circular. Although, as we show below (pp. 37–44), the

[27] Petitioners' reliance upon statements by Commission officials, such as the testimony of Chairman Cohen (Pet. Br., p. 26, fn. 32), that the bank's unit of participation is a "security" is misplaced. These statements refer to the securities laws and not to the Glass-Steagall Act.

bank activity of providing investment advice is entirely consistent with the purposes of the Glass-Steagall Act, petitioners contend that the addition of the wholly separate requirements of the securities laws (resulting in the issuance of "securities") creates a situation in which this activity is prohibited by the language of that Act. But for the definitions contained in the securities laws, however, there would be nothing that could possibly be a "security" under the Glass-Steagall Act. The application of the securities laws cannot make a commingled managing agency account illegal under the banking laws.

In any event, the extremely broad definition of the term "securities" in the Securities Act of 1933 should not be carried over to the Glass-Steagall Act. Judge Bazelon's analysis is compelling (App. 274):

> The words security and underwriter in the Securities Act of 1933 are terms of art with a high gloss. Their expansive definitions under the Securities Act cannot be imported wholesale into the Glass-Steagall Act when the two statutes serve different purposes, in different contexts of risk to the public. The securities laws are intended to protect investors primarily through disclosure requirements. Their terms have been interpreted broadly to afford their protection to purchasers of all manner of investment interests, wherever it is needed. The Glass-Steagall Act, by contrast, was enacted to protect bank depositors and the banking system from the risk of insolvency incident to widespread investment of banks' assets in speculative securities during the twenties. * * *

Petitioners' contention that the term "securities" has the same meaning in Glass-Steagall as in the federal securities laws not only ignores the differing legislative objectives of these two enactments (see *supra*, pp. 25–28, 36), but would go far beyond outlawing commingled managing agency accounts. The definition of "security" in the Securities Act of 1933 and the Securities Exchange Act of 1934, 15 U.S.C. 77b, 78c(a)(10), would cover many banking transactions, such as the issuance of a savings and loan association passbook (*Tcherepnin* v. *Knight*, 389 U.S. 332) and the sale by a bank of a loan participation (*Lehigh Valley Trust Co.* v. *Central National Bank of Jacksonville*, 409 F. 2d 989 (C.A. 5)). Since these interests have been held to be "securities" under the federal securities laws, under petitioners' theory they could not be issued by a banking institution because of the proscriptions of the Glass-Steagall Act. Congress did not intend such a result to flow from the enactment of the latter statute.

B. THE GLASS-STEAGALL ACT WAS NOT INTENDED TO PREVENT BANKS FROM OFFERING THEIR FIDUCIARY INVESTMENT ADVISORY SERVICES TO A WIDER RANGE OF CUSTOMERS

As we have shown above, the issuance of certificates representing participating interests in the Account is not dealing in "securities" within the meaning of the Glass-Steagall Act merely because the certificates are technically securities under the securities laws. We now show that the operation of the Account is consistent with the purposes of that Act.

The legislative history of the Glass-Steagall Banking Act of 1933, some of which we have summarized

in Appendix B to this brief, demonstrates that Congress was concerned in that Act with the problems inherent in the intermingling of commercial and investment banking. In the securities provisions of the Glass-Steagall Act, as noted above, *supra,* pp. 25–28, Congress attempted to safeguard commercial banks from making excessively speculative financial commitments, which were fraught with potential conflict of interest problems, by prohibiting banks from purchasing, issuing, and underwriting many types of securities. The Act was especially concerned with the conflicts of interest inherent in the relationship between commercial banks and their securities affiliates, which were organizations established to circumvent prior laws prohibiting commercial banks from entering the investment banking business, and which used the bank's funds for "perilous underwriting operations, stock speculation, and maintaining a market for the bank's own stock * * *" Sen. Rep. No. 77, 73d Cong., 1st Sess. p. 10 (1933).[28]

The Glass-Steagall Act was in no way intended to limit the traditional function of banks to manage the investments of their customers in a fiduciary capacity.[29] The dangers of excessive speculative risk and the

[28] See our brief in No. 59, *NASD* v. *Securities and Exchange Commission*, pp. 18–19.

[29] Petitioners contend (Pet. Br. p. 52) that Congress would not have regarded the Bank's commingling of managing agency accounts as a fiduciary activity under 12 U.S.C. 92a because, in Section 584 of the Internal Revenue Code, Congress exempted from taxation only common trust funds maintained by a bank in its capacity as "trustee, executor, administrator, or guardian." However, the predecessor of Section 584 (Section 169 of the

resultant conflict of interest which Congress intended to prevent when it passed that Act are simply not present when banks manage investment accounts in which the bank's interest is limited to its advisory fee.[30] From the standpoint of the Glass-Steagall Act, it makes no difference whether funds managed by the bank are commingled in order to extend the bank's services to a wider range of customers.

As the majority concurring opinion below pointed out, "[i]n one form or another banks have been holding, managing and investing funds for customers for a long time" (App. 310). For example, at least since 1934, when the Federal Reserve Board and the Comptroller of the Currency specifically approved the practice, national banks have acted as managing agents in buying, selling, and holding common stock or other securities for the account of individual bank customers pursuant to an agreement making the bank the customer's agent (see p. 4, *supra*). In addition, since 1915 national banks have managed trust accounts containing securities (38 Stat. 262; 1 Fed. Reserve Bull. 43 (1915)), and, since 1937, have been permitted to commingle the assets of such accounts and to administer them in a common trust fund (see p. 4,

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Revenue Act of 1936) was enacted in 1936 to meet the specific problems arising from the decision in *Brooklyn Trust Co.* v. *Commissioner*, 80 F. 2d 865 (C.A. 2), certiorari denied, 298 U.S. 659 (1936), and the treatment of managing agency funds was not expressly considered (see Saxon and Miller, *Common Trust Funds*, 53 Geo. L.J. 994, 1003–1009 (1965)).

[30] The Comptroller prohibits a bank administering a collective investment fund from having any direct interest in such a fund (12 C.F.R. 9.18(b)(8)(i)).

supra).[31] Similarly, since 1955 banks have been permitted to administer commingled pension, profit share, or stock bonus plan funds—some of which have been held by banks in the capacity of managing agent. 20 F.R. 3305 (1955). Petitioners do not, and cannot, object to the legality of these longstanding bank services.

Nor is there anything novel in the concept or in the practical operation of a commingled managing agency investment account. Such an account is designed simply to make available to the smaller investor (in this case one with $10,000 to invest) the benefit, previously available only to large investors through individual managing agency accounts, of having their investments managed by a bank trust department.[32] As Judge Bazelon pointed out below, the fact that the bank's services are now available to a wider range of customers in no way alters the relationship be-

[31] In fact, such funds were approved as early as 1927 by the Comptroller and the Federal Reserve Board. See the description of the Security National Bank Bond Investment Trust in Saxon and Miller, *Common Trust Funds*, 53 Geo. L.J. 994, 997 (1965).

[32] Petitioners devote considerable attention (Br. pp. 49–55) to refuting a contention never made by any party in this litigation—that the commingled managing account is "immune" from the Glass-Steagall Act "simply because it is operated by the Bank's trust department." The Comptroller's position has always been that the operation of the commingled managing account is within the fiduciary powers granted national banks by 12 U.S.C. 92a and consistent with the prohibitions of the Glass-Steagall Act against bank investment in the securities business; the Comptroller does not claim a "license to violate the provisions of substantive law."

tween investment advisory services and the Glass-Steagall Act.[33]

> The establishment of a bank-sponsored collective investment fund is not barred by the banking laws. A commingled managing agency account is a descendant of the individual managing agency account and the common trust fund, fitting within the traditional authority of banks to manage other people's money in a fiduciary capacity sanctioned by the Federal Reserve Act. * * * The sale of an investment service to a potentially large number of customers gives rise to obligations under the securities laws, but these do not convert otherwise lawful transactions for the account of customers into prohibited securities dealings within the meaning of the Glass-Steagall Act. [App. 278.]

In support of his conclusion that the Account presents no potential problems which are not present "in

[33] Petitioners assert (Pet. Br. 22, fn. 28) that "The prohibitions of the Glass-Steagall Act were understood at the time of the Act's passage to bar relationships between a bank and an investment fund of the type authorized by the Comptroller's Regulation." However, the Irving Investor's Fund C described in petitioners' brief (p. 22, fn. 28) was not comparable to the commingled account now operated by the Bank, so that the experience of the Irving Trust Company does not support petitioners' contention concerning the Glass-Steagall Act. Irving Fund C was a separate corporate entity, which issued shares directly to the public. There does not appear to have been a fiduciary relationship between the shareholders and the Irving Trust Company, as is required for admission to the Account. More comparable to the Bank's present commingled account was the Brooklyn Trust Company's Composite Fund, Series A, which continued to be operated by Brooklyn Trust Company after the passage of the Glass-Steagall Act. See *Saxon and Miller*, *supra*, n. 31, at 999–1000, 1003–1009.

all bank investments in securities for the account of customers" (App. 275), Judge Bazelon analyzed in detail the specific problems at which Sections 16, 20, 21, and 32 of the Glass-Steagall Act were aimed. He concluded, for example, that Sections 16 and 21, which essentially prohibit banks from issuing or underwriting securities, were addressed to three problems—risky investments of bank assets, the making of unsound loans to shore up companies in which the bank had invested, and the incentive to "steer" customers into investing what the bank has to sell.

With respect to the first of these problems, risky investments of bank assets, Judge Bazelon correctly pointed out that it "does not arise here, because the securities in the fund are purchased for the account of the customer, not the bank" (App. 275). With respect to the second danger, shoring up bad investments with unsound loans, Judge Bazelon pointed out that the risk is significantly reduced by virtue of the fact that the securities are not held for the Bank's own account, and, again, that whatever risk remains is no different from that always present in bank-managed investment accounts. As for the third problem, the bank's incentive to steer customers into investing in the Account, Judge Bazelon noted that "The Bank's interest in earning a regulated fiduciary charge bears little resemblance to its interest in earning an indeterminate distributing profit from securities which it owns or underwrites, and the interest forbidden by § 16 is the latter" (App. 275–276). Similarly, with respect to Sections 20 and 32 of the Act, which prohibit various interlocks and affiliations

of personnel between banks and securities dealers, Judge Bazelon noted that "The clear purpose of §§ 20 and 32 is to prevent banks from entering into prohibited forms of securities dealing by the back door. We have held that the Bank may enter the business of operating the Account by the front door" (App. 277).

Petitioners' argument ignores the critical consideration, which Judge Bazelon persuasively developed, that the potential risks and conflicts of interest here are no greater than in the case of any other fiduciary account. Petitioners argue (Br. 34–37), for example, that the Bank will be under pressure to merchandise the fund "aggressively" because its fee depends upon the size of the Account;[34] that "in order to maintain the fund's value," the Bank might "make loans needed by companies whose stock is held" by the Account; that a poor performance by the Account might undermine public confidence in the Bank; and even that the Bank might change the prime rate of

[34] To support this contention, petitioners cite (Br. 34) the statement of former Chairman Cary of the Commission that the transfer of participations in the Account involved a "public offering." Chairman Cary obviously was referring not to the merchandising practice of the banks, but to the phrase "offered to the public" as used in Section 4 of the Securities Act of 1933, 15 U.S.C. 77d, on the basis of which the Commission asserted jurisdiction over the Account. The Comptroller's regulation prohibits advertising a collective investment account, except in connection with the Bank's general fiduciary services, and limits the Bank's publicizing of its investment record (12 C.F.R. 9.18(b)(5)(iii) and (iv)). Moreover, as Judge Bazelon's opinion noted, "* * * the merchandising problem is more relevant to the question of the proper exercise of fiduciary powers than to entry into the securities business within the meaning of the Glass-Steagall Act." (App. 275).

interest in order to affect the value of the securities held by the Account. Petitioners do not attempt to explain how the potential evils they envision are distinguishable from those present, for example, in the ordinary trust account.[35] Petitioners argument thus rests upon a fundamental misconception of the function of the Glass-Steagall Act.[36]

III

AUTHORIZATION OF COMMINGLED MANAGING AGENCY ACCOUNTS WAS A PROPER EXERCISE OF THE COMPTROLLER'S REGULATORY POWERS

As we have shown, operation of commingled managing agency accounts is not inconsistent with the purposes of the applicable banking statutes. Once this has been determined, the complex questions about the appropriateness of these accounts in general and the

[35] Petitioners also contend that the Bank might make unsound loans directly to the Account. The Comptroller's regulations, however, foreclose such a possibility by prohibiting a bank that administers a commingled fiduciary account from having "any interest in such fund other than in its fiduciary capacity * * *" 12 C.F.R. 9.18(b)(8)(i). In addition, the Account's prospectus states that it will not borrow money (App. 148).

[36] Petitioners also discern a conflict between the interests of the Account and those of the Bank in the fact that the Account "represents a potential for bringing under bank control substantial amounts of voting securities over and above the vast amounts now held in bank trust departments" (Br. 38–39). We do not understand, nor have petitioners explained, how such a "potential" bears upon a conflict of interest between the Account and the Bank, such as concerned Congress in enacting the Glass-Steagall Act. Bank control of voting shares would, instead, seem to be a matter of concern for the antitrust laws. See *United States* v. *Cleveland Trust Co.*, N.D. Ohio, Civil Action No. C70.301 (complaint filed March 26, 1970).

circumstances and conditions under which they should be permitted are questions for the regulatory agencies charged with administration of the banking laws. Courts should not interfere with the expert judgment of these agencies when they act within their statutory authority. *Unemployment Compensation Commission* v. *Aragon,* 329 U.S. 143, 153–154; *Federal Security Administrator* v. *Quaker Oats Co.,* 318 U.S. 218, 233; *Inland Waterways Corp.* v. *Young,* 309 U.S. 517, 524. Furthermore, the Comptroller's interpretation of the statute which he administers is entitled to great weight. *National Labor Relations Board* v. *Hearst Publications,* 322 U.S. 111, 131.

Recognizing that the Comptroller, the Federal Reserve Board, and the Commission,[37] after careful and

[37] Petitioners suggest several times that the Comptroller's regulations are contrary to previous rulings of the Federal Reserve Board (Br. pp. 9, 29, 32, fn. 38), and that therefore the regulatory agencies involved are in "disarray" over the lawfulness of the fund (Br. 10). In fact, the Federal Reserve Board has ruled only once on the legality of commingled managing agency accounts, in connection with this case, and that ruling supports the Comptroller's regulation. 12 C.F.R. 218.111. The Board has issued several opinions which apply Section 32 of the Glass-Steagall Act to prohibit interlocking relations between banks and certain *outside*, non-bank enterprises, which the Board found to be "double entities" (see Pet. Br. p. 32, fn. 38), but those opinions have no relevance here, because in this case the Board found that the Bank and the Account were a "single entity," 12 C.F.R. 218.111. The Board has similarly concluded that the single-entity theory applies in the case of the functionally similar common trust funds and various pooled funds, including employee pension or profit-sharing trusts. See Hearings on S. 2704, before a Subcommittee of the Senate Committee on Banking and Currency, 89th Cong., 2d Sess., p. 586 (1966).

extensive consideration, have unanimously approved the establishment of commingled managing agency accounts,[38] Judge Burger concluded as follows (App. 310):

> Here the Comptroller of the Currency, after study, has decided that the commingled managing agency account is a function which is authorized by law for banks and is in the public

[38] Congress has also had occasion to consider this matter. S. 2224, passed by the Senate on May 26, 1969, specifically authorizes operation of the commingled managing agency account here involved, while H.R. 6778, passed by the House of Representatives on November 5, 1969, apparently specifically prohibits the operation of such an account.

There is no support for petitioner's statement (Pet. Br., p. 27) that "the Senate and House Committees on Banking and Currency are also of the view that a bank open-end investment fund like that of Citibank's is engaged in the 'underwriting, distribution and sales of securities' for the purposes of the banking and securities laws". The Senate Committee report cited for this proposition does recognize that the units of participation are "securities" within the meaning of the securities laws. As to the banking laws, however, the Senate report stated that the district court's decision in this case "held that the Glass-Steagall Act prohibited banks from selling interests in collective investment funds to the general public." The committee characterized the district court's decision as reviving the "prior unfortunate confusion" and creating "an unwarranted comparative disparity" between the ability of banks and of mutual funds to offer investment advice to the public. S. Rep. No. 91-184, 91st Cong., 1st Sess., 11 (1969). The House Committee report cited by petitioners included "prevailing views" and "additional views". The statement concerning the Glass-Steagall Act relied upon by petitioners is found in the additional views which were not adopted by a majority of the Committee. Thus neither the Senate nor the House Banking and Currency Committee has expressed any view in connection with its consideration of current legislation concerning the applicability of the Glass-Steagall Act to a commingled fund such as that of the Bank.

> interest; the Securities and Exchange Commission and the Federal Reserve Board have approved. Other state and federal regulatory bodies are in accord. The regulatory bodies charged by Congress with these large responsibilities have construed the grant of power and with their accumulated expert experience have decided these issues. Their decisions are entitled to substantial deference and on this record I see no basis for disturbing their conclusions.

Judge Burger's conclusion that the Comptroller's regulations and his authorization of the Bank's operation of the Account are appropriate exercises of that official's supervisory power over the fiduciary activities of banks under Section 92a [39] of Title 12 reflects the application of the settled principles of administrative law noted above. There is no occasion for this Court to disturb those determinations of the Comptroller.

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[39] Section 92a(j) of Title 12 authorizes the Comptroller to "promulgate such regulations as he may deem necessary to enforce compliance with the provisions of this section and the proper exercise of the powers granted therein."

CONCLUSION

For the reasons stated, we respectfully submit that the judgment of the court of appeals should be affirmed.

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APPENDIX A

STATUTES AND REGULATIONS INVOLVED

1. Sections 16, 20, 21 and 32 of the Glass-Steagall Banking Act of 1933, 48 Stat. 184–85, 188–89, 194, as amended, 49 Stat. 707, 709 (1935), 12 U.S.C. §§ 24, 377, 378, 78 (1964) provide in pertinent part:

> SEC. 16. Paragraph "Seventh" of section 5136 of the Revised Statutes, as amended (U.S.C. title 12, sec. 24; Supp. vi, title 12, sec. 24), is amended to read as follows:
>
> "Seventh. To exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discontinuing and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing and circulating notes according to the provisions of this chapter. The business of dealing in securities and stock by the association shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the association shall not underwrite any issue of securities or stock: *Provided,* That the association may purchase for its own account investment securities under such limitations and restrictions as the Comptroller of the Currency may by regulation prescribe. In no event shall the total amount of the investment securities of any one obligor or maker, held by the asso-

ciation for its own account, exceed at any time 10 per centum of its capital stock actually paid in and unimpaired and 10 per centum of its unimpaired surplus fund, except that this limitation shall not require any association to dispose of any securities lawfully held by it on August 23, 1935. As used in this section the term "investment securities" shall mean marketable obligations, evidencing indebtedness of any person, copartnership, association, or corporation in the form of bonds, notes and/or debentures commonly known as investment securities under such further definition of the term "investment securities" as may by regulation be prescribed by the Comptroller of the Currency. Except as hereinafter provided or otherwise permitted by law, nothing herein contained shall authorize the purchase by the association for its own account of any shares of stock of any corporation. * * *

SEC. 20. (a) After one year from the date of the enactment of this Act, no member bank shall be affiliated in any manner described in section 2(b) hereof with any corporation, association, business trust, or other similar organization engaged principally in the issue, flotation, underwriting, public sale, or distribution at wholesale or retail or through syndicate participation of stocks, bonds, debentures, notes, or other securities: * * *.

* * * * *

SEC. 21. (a) After the expiration of one year after June 16, 1933, it shall be unlawful—

(1) For any person, firm, corporation, association, business trust, or other similar organization, engaged in the business of issuing, underwriting, selling or distributing, at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes, or other securities, to engage at the same time to any extent whatever in the business of receiving deposits subject to check or to repayment upon

presentation of a passbook, certificate of deposit, or other evidence of debt, or upon request of the depositor: *Provided*, That the provisions of this paragraph shall not prohibit national banks or State banks or trust companies (whether or not members of the Federal Reserve System) or other financial institutions or private bankers from dealing in, underwriting, purchasing, and selling investment securities to the extent permitted to national banking associations by the provisions of section 24 of this title: * * *

* * * * *

SEC. 32. No officer, director, or employee of any corporation or unincorporated association, no partner or employee of any partnership, and no individual, primarily engaged in the issue, flotation, underwriting, public sale, or distribution, at wholesale or retail, or through syndicate participation, of stocks, bonds, or other similar securities, shall serve the same time as an officer, director, or employee of any member bank except in limited classes of cases in which the Board of Governors of the Federal Reserve System may allow such service by general regulations when in the judgment of the said Board it would not unduly influence the investment policies of such member bank or the advice it gives its customers regarding investments.

* * * * *

2. Public Law 87–722, 76 Stat. 668 (1962), 12 U.S.C. 92a (1964) provides in pertinent part:

(a) The Comptroller of the Currency shall be authorized and empowered to grant by special permit to national banks applying therefor, when not in contravention of State or local law, the right to act as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, committee of estates of lunatics, or in any other fiduciary capacity in which State banks, trust companies, or other

corporations which come into competition with national banks are permitted to act under the laws of the State in which the national bank is located.

* * * * *

(j) * * * The Comptroller of the Currency is authorized and empowered to promulgate such regulations as he may deem necessary to enforce compliance with the provisions of this section and the proper exercise of the powers granted therein.

3. Regulation 9 of the Comptroller of the Currency, 12 C.F.R. § 9 (1967), provides in pertinent part:

§ 9.18 Collective investment.

(a) Where not in contravention of local law, funds held by a national bank as fiduciary may be invested collectively:

(1) In a common trust fund maintained by the bank exclusively for the collective investment and reinvestment of monies contributed thereto by the bank in its capacity as executor, administrator, guardian or trustee under a will or deed;

(2) In a fund consisting solely of assets of retirement, pension, profit sharing, stock bonus, or other trusts which are exempt from Federal income taxation under the Internal Revenue Code;

(3) In a common trust fund, maintained by the bank exclusively for the collective investment and reinvestment of monies contributed thereto by the bank in its capacity as managing agent under a managing agency agreement expressly providing that such monies are received by the bank in trust;

(b) Collective investments of funds or other property by national banks under paragraph (a) of this section (referred to in this paragraph as "collective investment funds") shall be administered as follows:

(1) Each collective investment fund shall be established and maintained in accordance with a written plan (referred to herein as the Plan) which shall be approved by a resolution of the bank's board of directors and filed with the Comptroller of the Currency. The Plan shall contain appropriate provisions not inconsistent with the rules and regulations of the Comptroller of the Currency as to the manner in which the fund is to be operated, including provisions relating to the investment powers of the bank with respect to the fund, the allocation of income, profits and losses, the terms and conditions governing the admission or withdrawal of participations in the fund, the auditing of accounts of the bank with respect to the fund, the basis and method of valuing assets in the fund, the minimum frequency for valuation of assets of the fund, the period following each such valuation date during which the valuation may be made, the basis upon which the fund may be terminated, and such other matters as may be necessary to define clearly the rights of participants in the fund: *Provided,* That Plans which have been established in conformance with prior regulations of the Board of Governors of the Federal Reserve System or the Comptroller of the Currency may continue to conform to such regulations rather than the requirements of this paragraph, for a reasonable period. A copy of the Plan shall be available at the principal office of the bank for inspection during all banking hours, and upon request a copy of the Plan shall be furnished, to any person.

(2) Monies held by the bank in its capacity as managing agent shall not be invested in collective investment funds established under the provisions of paragraph (a) (1) or (2) of this section. Property held by the bank in its capacity as trustee of retirement, pension, profit sharing, stock bonus or other trusts

which are exempt from Federal income taxation under the Internal Revenue Code may be invested in collective investment funds established under the provisions of paragraph (a) (1) or (2) of this section, subject to the provisions herein contained pertaining to such funds. Assets of retirement, pension, profit sharing, stock bonus or other trusts which are exempt from Federal income taxation under the Internal Revenue Code and held by the bank, in whatever capacity, may be invested in collective investment funds established under the provisions of paragraph (a)(2) of this section.

(3) All participations in the collective investment fund shall be on the basis of a proportionate interest in all of the assets. In order to determine whether the investment of funds received or held by the bank as fiduciary in a participation in a collective investment fund is proper, the bank may consider the collective investment fund as a whole and shall not, for example, be prohibited from making such investment because any particular asset is non-income producing.

(4) Not less frequently than once during each period of three months a bank administering a collective investment fund shall determine the value of the assets in the fund as of the dates set for the valuation of assets. No participation shall be admitted to or withdrawn from the fund except (i) on the basis of such valuation and (ii) as of such valuation date. No participation shall be admitted to or withdrawn from the fund unless a written request for or notice of intention of taking such action shall have been entered on or before the valuation date in the fiduciary records of the bank and approved in such manner as the board of directors shall prescribe. No such request or notice may be cancelled or countermanded after the valuation date.

(5)(i) A bank administering a collective investment fund shall at least once during each period of 12 months cause an adequate audit to be made of the collective investment fund by auditors responsible only to the board of directors of the bank. In the event such audit is performed by independent public accountants, the reasonable expenses of such audit may be charged to the collective investment fund.

(ii) A bank administering a collective investment fund shall at least once during each period of 12 months prepare a financial report of the fund which shall be filed with the Comptroller of the Currency. This report, based upon the above audit, shall contain a list of the investments in the fund showing the current market value of each investment, a statement for the period since the last report showing purchases, sales and any other investment changes, income and disbursements, and an appropriate notation as to any investment in default.

(iii) The financial report may include a description of the fund's value on previous dates as well as its income and disbursements during previous accounting periods. The report shall make no reference to the performance of funds other than those administered by the bank, and no predictions or representations as to future results.

(iv) A copy of the financial report shall be furnished, or notice shall be given that a copy of such report is available and will be furnished without charge upon request, to each person to whom a regular periodic accounting would ordinarily be rendered with respect to each participating account. The report, in such summarized form as prescribed by the Comptroller of the Currency, shall be published in a newspaper of general circulation in the place where the principal office of the bank is located. In addition,

a full report shall be furnished upon request to any person, and the fact of the availability of such material may be given publicity solely in connection with the promotion of the fiduciary services of the bank. Except as herein provided, the bank shall not advertise or publicize its collective investment fund(s). The cost of printing, publication and distribution of the report shall be borne by the bank.

(6) When participations are withdrawn from a collective investment fund, distributions may be made in cash or ratably in kind, or partly in cash and partly in kind, provided that all distributions as of any one valuation date shall be made on the same basis.

(7) If for any reason an investment is withdrawn in kind from a collective investment fund for the benefit of all participants in the fund at the time of such withdrawal and such investment is not distributed ratably in kind, it shall be segregated and administered or realized upon for the benefit ratably of all participants in the collective investment fund at the time of withdrawal.

(8) (i) A bank administering a collective investment fund shall not (*a*) have any interest in such fund other than in its fiduciary capacity (funds held by a bank as fiduciary as described under paragraph (a) (1) or (2) of this section for its own employees may be invested in such a fund) or (*b*) make any loans on the security of a participation in such fund. If because of a creditor relationship or otherwise the bank acquires an interest in a participation in such fund, the participation shall be withdrawn on the first date on which such withdrawal can be effected. However, in no case shall an unsecured advance to an account holding a participation until the time of the next withdrawal be deemed to constitute the acquisition of an interest by the bank.

(ii) The bank may purchase for its own account from a collective investment fund any defaulted mortgage held by such fund, if in the judgment of the board of directors the cost of segregation of such mortgage would be greater than the difference between its market value and its principal amount plus interest and penalty charges due. If the bank elects to so purchase the mortgage it must do so at its market value or at the sum of principal, interest and penalty charges, whichever is greater.

(9) Except in the case of collective investment funds described in paragraph (a)(2) of this section:

(i) No funds or other property shall be invested in a participation in a collective investment fund if as a result of such investment the participant would have an interest aggregating in excess of ten per cent of the then market value of the fund: *Provided,* That in applying this limitation if two or more accounts are created by the same person or persons and as much as one-half of the income or principal of each account is payable or applicable to the use of the same person or persons, such accounts shall be considered as one;

(ii) No investment for a collective investment fund shall be made in stocks, bonds or other obligations of any one person, firm or corporation if as a result of such investment the total amount invested in stocks, bonds or other obligations issued or guaranteed by such person, firm or corporation would aggregate in excess of ten percent of the then market value of the fund: *Provided,* That this limitation shall not apply to investments in direct obligations of the United States or other obligations fully guaranteed by the United States as to principal and interest;

(ii) Any bank administering a collective investment fund shall have the responsibility of maintain-

ing in cash and readily marketable investments such part of the assets of the fund as shall be deemed to be necessary to provide adequately for the needs of participants and to prevent inequities between such participants, and if prior to any admissions to or withdrawals from a fund the bank shall determine that after effecting the admissions and withdrawals which are to be made less than 40 percent of the value of the remaining assets of the collective investment fund would be composed of cash and readily marketable investments, no admissions to or withdrawals from the fund shall be permitted as of the valuation date upon which such determination is made: *Provided,* That ratable distribution upon all participations shall not be so prohibited in any case.

(10) The reasonable expenses incurred in servicing mortgages held by a collective investment fund may be charged against the income account of the fund and paid to servicing agents, including the bank administering the fund.

(11) (i) A bank may (but shall not be required to) transfer up to five percent of the net income derived by a collective investment fund from mortgages held by such fund during any regular accounting period to a reserve account: *Provided,* That no such transfers shall be made which would cause the amount in such account to exceed one percent of the outstanding principal amount of all mortgages held in the fund. The amount of such reserve account, if established, shall be deducted from the assets of the fund in determining the fair market value of the fund for the purposes of admissions and withdrawals.

(ii) At the end of each accounting period, all interest payments which are due but unpaid with respect to mortgages in the fund shall be charged

against such reserve account to the extent available and credited to income distributed to participants. In the event of subsequent recovery of such interest payments by the fund, the reserve account shall be credited with that amount so recovered.

(iii) Notwithstanding anything herein contained to the contrary, Mortgage Investment Funds presently being operated pursuant to the provisions of section 17(d) of prior regulations of the Comptroller of the Currency or the Board of Governors of the Federal Reserve System may continue to be operated in accordance with such prior regulations for a reasonable time. However, after April 5, 1963, no such funds shall be established.

(12) A national bank administering a collective investment fund shall have the exclusive management thereof. The bank may charge a fee for the management of the collective investment fund provided that the fractional part of such fee proportionate to the interest of each participant shall not, when added to any other compensations charged by the bank to the participant, exceed the total amount of compensations which would have been charged to said participant if no assets of said participant had been invested in participations in the fund. The bank shall absorb the costs of establishing or reorganizing a collective investment fund.

(13) No bank administering a collective investment fund shall issue any certificate or other document evidencing a direct or indirect interest in such fund in any form.

(14) No mistake made in good faith and in the exercise of due care in connection with the administration of a collective investment fund shall be deemed to be a violation of this part if promptly after the dis-

covery of the mistake the bank takes whatever action may be practicable in the circumstances to remedy the mistake.

(c) In addition to the investments permitted under paragraph (a) of this section, funds or other property received or held by a national bank as fiduciary may be invested collectively, to the extent not prohibited by local law, as follows:

(1) In shares of a mutual trust investment company, organized and operated pursuant to a statute that specifically authorizes the organization of such companies exclusively for the investment of funds held by corporate fiduciaries, commonly referred to as a "bank fiduciary fund".

(2) In a single real estate loan or a direct obligation of the United States, or an obligation fully guaranteed by the United States, if the bank owns no participation in the loan or obligation and has no interest therein except in its capacity as fiduciary.

(3) In a common trust fund maintained by the bank for the collective investment of cash balances received or held by a bank in its capacity as trustee, executor, administrator or guardian, which the bank considers to be individually too small to be invested separately to advantage, and the total investment in which on the part of any one account does not exceed $10,000: *Provided,* That in applying this limitation if two or more accounts are created by the same person or persons and as much as one-half of the income or principal of each account is payable or applicable to the use of the same person or persons, such account shall be considered as one: *And provided,* That no fund shall be established or operated under this subparagraph for the purpose of avoiding the provisions of paragraph (b) of this section.

(4) In any investment specifically authorized by court order or authorized by the instrument creating the fiduciary relationship: *Provided,* That such investment is not made under this paragraph for the purpose of avoiding the provisions of paragraph (b) of this section.

(5) In such other manner as shall be approved in writing by the Comptroller of the Currency.

APPENDIX B

SUMMARY OF THE PROBLEMS WHICH LED TO THE ENACTMENT OF THE GLASS-STEAGALL BANKING ACT OF 1933

The legislative history of the Glass-Steagall Banking Act of 1933 demonstrates that Congress was concerned that the intermingling of commercial and investment banking and the practices of "security affiliates" threatened the maintenance of a sound national banking system by: (1) contributing to bank failures; (2) endangering the safety of bank deposits; (3) leading to conflicts of interest by bankers; (4) inducing the making of unsound bank loans; (5) impairing public confidence in the banking system; and (6) diverting the resources of the commercial banking system to speculative purposes never contemplated by Congress. The history does not, however, reflect any Congressional intention to prohibit the operation of a trust department by a national bank.

a. In describing the banking conditions which culminated in the economic breakdown of 1929, Senate Report No. 77, 73d Cong., 1st Sess., p. 8, that a "very fruitful cause of bank failures, especially within the past three years, has been the fact that the funds of various institutions have been so extensively 'tied up' in long-term investments." Moreover, the Senate Report continued (*ibid.*), "The growth of the investment portfolio of the bank itself has been greatly emphasized in importance by the organization of allied or affiliated companies under State laws, through which even more extensive advances and in-

vestments in the security market could be made." Senator Glass similarly stated during floor debates that "one of the greatest contributions to the unprecedented disaster which has caused this almost incurable depression was made by these bank affiliates. They sent out their high-pressure salesmen and literally filled the bank portfolios of this country with these investment securities." 75 Cong. Rec. 9887 (May 10, 1932).

b. Congress was also concerned about the losses to bank depositors resulting from investment of bank assets in securities whose value subsequently declined. See Sen. Rep. No. 77, *supra,* pp. 9–10; 75 Cong. Rec. 9905–06 (May 10, 1932) (remarks of Senator Walcott); 77 Cong. Rec. 3924 (May 22, 1933) (remarks of Rep. Green) "I hope this bill will put a stop to this orgy of speculation with depositors' funds throughout the United States and make safe in the future our bank deposits." Congress was also aware that bank depositors suffered great losses on securities which they purchased from security affiliates in reliance upon the relationship between the bank and its affiliate. See 77 Cong. Rec. 4028 (May 23, 1933) (remarks of Rep. Fish).

c. Congress was also very much concerned with the conflicts of interest which bankers were frequently faced with as a result of their intermingling of commercial and investment banking. Banks which acted as issuers or underwriters of securities had a pecuniary interest in selling those securities, which conflicted with their duty to give their customers disinterested investment advice. As Senator Bulkley stated (75 Cong. Rec. 9912, 9915 (May 10, 1932)):

> Obviously, the banker who has nothing to sell his depositors is much better qualified to advise disinterestedly and to regard diligently the safety of depositors than the banker who

> uses the list of depositors in his savings department to distribute circulars concerning the advantages of this, that, or the other investment on which the bank is to receive an originating profit or an underwriting profit or a distribution profit or a trading profit or any combination of such profits.
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> * * * If we want banking service to be strictly banking service, without the expectation of additional profits in selling something to customers, we must keep the banks out of the investment security business.
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> * * * it makes a divided interest in the allegiance of a bank to its customers, and * * * it is not in accord with what we know human nature to be to expect that a bank shall have securities for sale on which it makes a profit and at the same time be competent to advise its customers with respect to their investments. * * * [2b]

Large banks were also placed in a position of conflict of interest by their sales of securities to correspondent banks. Indeed, Congress was deeply disturbed by the pressure which large city banks exerted upon their correspondent banks to purchase such securities, which were frequently unsound. As Senator Glass stated, "It was because of that system of involuntary servitude that the great banks in the money centers choked the portfolios of their correspondent banks from Maine to California with utterly worthless investment securities * * *." 75 Cong. Rec. 9883 (May 10, 1932). See also 75 Cong. Rec. 9906 (May 10, 1932) (remarks of Senator Walcott) ("We have banks

[2b] Senator Glass similarly stated that bank engagement in the investment business was "a vain attempt to fairly serve two masters, and * * * it can not be done." 75 Cong. Rec. 9915 (May 10, 1932).

that have closed their doors because they have overpurchased, as correspondent banks of some of the larger ones, the very securities that the larger banks have forced upon them"); 75 Cong. Rec. 9978 (May 11, 1932) (remarks of Senator Norbeck).

There were also conflicts on "the other side of the picture." As Senator Bulkley stated (75 Cong. Rec. 9911–12, 9914—May 10, 1932):

> * * * Can any banker, imbued with the consciousness that his bond-sales department is, because of lack of securities for sale, losing money and at the same time losing its morale, be a fair and impartial judge as to the necessity and soundness for a new security issue which he knows he can readily distribute through channels which have been expensive to develop but which presently stand ready to absorb the proposed security issue and yield a handsome profit on the transaction?
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> * * * If, on the other hand, the business of originating and underwriting investment securities is confined to houses not engaged in deposit banking, than the extent and the desirability of new issues will be subjected to an independent and impartial check. This should tend to restore public confidence.
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> A corporation, having carried its account with a bank, having borrowed from that bank for its ordinary commercial requirements, is confronted with the question of raising long-term funds by the issuance of securities. If it is to have the advice of its banker untainted by the prospect of obtaining an originating or underwriting profit we must keep the banks out of the security business.

In addition to the prospect of an underwriting profit, a desire to avoid the effects of bad loans also impaired the impartial judgment of a number of

banks who had to evaluate the desirability of a securities issue by a loan customer. In the Glass-Steagall Act, Congress intended that "The public will be protected against the possibility of being offered bonds which represent bad banks loans or 'dirty linen' converted through a security affiliate." 75 Cong. Rec. 3954 (May 22, 1933) (remarks of Rep. Bacon). See also 75 Cong. Rec. 9912 (May 10, 1932) (remarks of Senator Bulkley): "If the public is to be protected against the possibility of bad bank loans being set up into bond issues to be sold to savings depositors of the same banks without the exacting scrutiny of an independent underwriter interested primarily in the soundness of the securities he is about to sell we must prohibit the banks from engaging in the security business."

Congress was also concerned that banks engaged in the securities business often suffered "the embarrassment of having to appraise, as collateral security offered by prospective borrowers, the very securities" which the banks or their affiliates had sold. 75 Cong. Rec. 9912, 9914 (May 10, 1932) (remarks of Senator Bulkley), 77 Cong. Rec. 3954 (May 22, 1933) (remarks of Senator Bacon).[1]

d. Congress was further concerned that direct bank investment in securities created pressure for banks to make unsound loans to companies to maintain the price of securities generally or the financial position of the borrower companies in which the banks had holdings. Unsound bank loans were also made to bank customers in order to finance the purchase by them of securities on which the lending bank made an originating or underwriting commission. Banks frequently

[1] The Comptroller's regulation governing the collective fund now before the Court provides: "A bank administering a collective investment fund shall not * * * (b) make any loans on the security of a participation in such fund." 12 C.F.R. 9.18(b)(8)(i).

made unsound loans to their security affiliates. As Senator Bulkley stated (75 Cong. Rec. 9911–12, 9914—May 10, 1932):

> * * * Can there be any doubt that in order to maintain the market conditions which would absorb the great production of capital securities and produce the big profits for the affiliates and bond departments commercial banks went astray by encouraging an overdevelopment of collateral-security loans? Is it not fair to attribute the vast development of loans on collateral security at least in part to the necessity for keeping up a market condition capable of absorbing capital issues? * * *
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> * * * If we are to keep banks from being tempted to make security loans in order to help make a market or to finance the purchase of securities on which the lending bank is making an originating or underwriting commission we must keep banks out of the investment security business. * * *
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> * * * We feel that by removing the bankers from the temptation of using credit in such a way as to make a good background and foundation for the flotation for more security issues we are protecting the depositors * * *.

See also Hearings Pursuant to S. Res. 71 before a Subcommittee of the Senate Committee on Banking and Currency, 71st Cong., 3d Sess., pp. 20, 237, 1017, 1066–67 (1931); 77 Cong. Rec. 3954 (May 22, 1933) (remarks of Rep. Bacon); Sen. Rep. No. 1455, 73d Cong., 2d Sess., p. 186 (1934).

e. Congress was disturbed that the abuses, described above, resulting from the intermingling of commercial and investment banking, had impaired public confidence in the banking system. Public confidence in

banks was also undermined by the losses experienced by security affiliates, who were closely associated with the banks in the public mind. By separating commercial from investment banking, and eliminating the interlocking relationships between banks and security affiliates, Congress sought to restore public confidence in the banking system. See, *e.g.*, 75 Cong. Rec. 9912, 9915 (May 10, 1932) (remarks of Senator Buckley); 75 Cong. Rec. 9981 (May 11, 1932) (remarks of Senator Norbeck); 77 Cong. Rec. 3835 (May 20, 1933) (remarks of Rep. Steagall); 77 Cong. Rec. 3907 (May 22, 1933) (remarks of Rep. Kopplemann).

f. Another central concern of Congress was that the investment business of banks, and their relationships with security affiliates, was diverting the resources of the commercial banking system to speculative purposes never contemplated by Congress. See Sen. Rep. No. 77, *supra*, p. 8:

> The outstanding development in the commercial banking system during the prepanic period was the appearance of excessive security loans, and of overinvestment in securities of all kinds. The effects of this situation in changing the whole character of the banking problem can hardly be overemphasized. National banks were never intended to undertake investment banking business on a large scale, and the whole tenor of legislation and administrative rulings concerning them has been away from recognition of such a growth in the direction of investment banking as legitimate. * * *

As Senator Glass stated (75 Cong. Rec. 9884—May 10, 1932):

> * * * In large degree the system has been transformed into an investment banking system, whereas the fixed purpose of Congress was to set up a commercial banking system and to preclude speculative operations.

Representative Steagall summed up the purposes of his bill in the following language (77 Cong. Rec. 3835 —May 20, 1933):

> The great Federal Reserve Act was enacted as a result of the lessons of experience gathered from conditions that existed in 1907 and prior to that time. Under the Federal Reserve Act we experienced a period of progress and prosperity unparalleled in all our history. Under that act we financed the greatest war in all the tide of time and emerged from that conflict the financial center of the world and the dominating force in the diplomacies of mankind. Under that act credit facilities have been afforded for domestic purposes and also a large measure of the credit requirement for international trade and business.
>
> But we seemed to forget the lessons of experience. We departed from sound banking principles. Our great banking system was diverted from its original purposes into investment activities, and its service devoted to speculation and international high finance. Our financial leaders went on a spree. They cranked up our great financial machine, charged it with high-powered gas, and soared away toward the heavens, forgetting that there would ever be need for a place to land or that a wreck awaited them. Agriculture, commerce, and industry were forgotten. Bank deposits and credit resources were funneled into the speculative centers of the country for investment in stocks operation and in market speculation. Values were lifted to fictitious levels. Call-money rates went soaring, community bankers over the Nation were lured away from normal and legitimate channels into a maelstrom of untried and destructive activities.
>
> Bankers engaged in extending credits for legitimate purposes, for loans in support of commerce and agriculture and for community service and the development of community life,

were urged to abandon this service and place their investments in what were represented to them as sound and liquid securities. A campaign was turned on urging bankers everywhere to take out of their portfolios papers representing the collateral and the character of local citizens and to employ their facilities in investment banking, in speculation, in stock gambling, and in aid of wild and reckless international high finance.

The purpose of the regulatory provisions of this bill is to call back to the service of agriculture and commerce and industry the bank credit and the bank service designed by the framers of the Federal Reserve Act.

The purpose is to strengthen the banking structure, to establish adequate capital requirements, to provide more effective regulation and supervision, to eliminate dangerous and unsound practices, and to confine banks of deposit to legitimate functions and to separate them from affiliates or other organizations which have brought discredit and loss of public confidence. We propose to see to it that hereafter the credit facilities of the Federal Reserve System shall be devoted primarily to the purposes to which that great act was dedicated at the outset.

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Vide No. 59 for (3) related briefs.